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Dairy and Products

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Report Highlights:

Indonesian fresh milk production remains stagnant at 1.2 million liters per day and meeting about 25 percent of Indonesian demand for milk. The gap is fulfilled from imports. Despite the soaring price of non fat dry milk as well as whole milk powder in the international market, imports of non fat dry milk are forecast to continue growing to 161 TMT in 2008 as demand remain firm, while imports of whole milk powder are forecast to be stable at 27 TMT in 2008.

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I. SITUATION AND OUTLOOK

The Indonesian milk processing industry is expected to continue growing. Despite the soaring price of milk powder in the international market, imports of non-fat dry milk are estimated to increase by 9.5 percent to 161,000 tons due to strong demand, and imports of whole milk powder are estimated to remain on par at 27,000 tons in 2008. The severe drought in Australia and EU's policy to eliminate export subsidies will result in increased imports of U.S. dairy products.

Inefficient small-scale farms and poor farming practices continue to hinder further improvement in Indonesian milk production and milk quality. The high price of powdered milk in the international market has tightened the competition among the major Indonesian dairy processing companies to get their fresh milk from dairy cooperatives.

The Indonesian economy is expected to improve again in 2007. Economic growth is estimated to reach 6.3 percent, inflation at 6.5 percent, and the currency exchange is expected to remain stable at around Rp. 9,000 per US\$ 1.

PRODUCTION

In 2007, Indonesian fresh milk production will remain relatively stagnant at 1.2 million liters per day equal to 48 TMT, and can only meet 25 percent of overall Indonesian milk demand. Indonesian milk production is sourced from around 320,000 cattle largely located in three milk-producing areas in Java. West Java's dairy cooperatives used to produce the highest amount of milk, but the position was taken over by East Java's dairy cooperatives in 2004 when the price of beef skyrocketed so that farmers received more from culling their dairy cattle for beef versus looking after the cattle for milk. Currently West Java's dairy cooperative produces approximately 400,000 liters of milk per day while East Java produces 600,000 liters of milk per day. The balance is produced by Central Java and other parts of Indonesia.

Milk quality as measured by bacteria content (TPC = Total Plate Count) also remains low at an average bacteria content ranging from 500,000 – 1 million per ml. Most of Indonesian fresh milk production is combined with non-fat dry milk to produce full cream liquid and powdered milk. Fresh milk with higher TPC is used as a raw material to produce sweetened condensed milk. Further efforts to improve milk production and milk quality are hampered by several fundamental problems, including the low level of farmer education, the small size of farms, poor farming and hygiene practices, the scarcity of water, the scarcity of feed and forage, the scarcity of land with suitable elevation for dairy farms, lack of incentives for farmers, the number of times that fresh milk is handled before it reaches the consumers, and the lack of technology. Government also only pays minimal attention to this sector.

Farmers also find difficulties in finding qualified dairy genetics since there are only two agencies that provide semen for artificial insemination, in Lembang, West Java and in Malang, East Java. There are no dairy cattle breeders in Indonesia. The two stations used to import semen from Canada however since the outbreak of BSE semen is no longer imported from Canada. Farmers now buy calves locally priced at half the price of imported dairy cattle.

In contrast to the small scale and inefficient milk production units, large and efficient companies dominate the milk-processing sector. The low level of Indonesian per capita milk consumption provides opportunities for new processors to enter the market. Two major snack food companies are expected to begin milk production in 2008. The dairy and dairy

products market is expected to grow by 12-15 percent annually however the high price of powdered milk in the international market may hinder growth.

On January 8, 2007 GoI issued Government of Indonesia's Regulation No. 7/2007 which eliminates the 10 percent Value Added Tax on certain strategic taxable goods including chilled non concentrated unsweetened pasteurized fresh milk. This policy is expected to improve Indonesian milk processor's cash flow.

CONSUMPTION

Total Indonesian milk consumption is estimated to increase by 6 percent in 2008. Indonesian per capita milk consumption is estimated to increase to 7.7 kg/year in 2007 mostly due to the increased awareness of the health benefits of milk. However, the soaring price of milk powder in the international market has forced the Indonesian dairy industry to increase the price of their dairy finished products gradually up to 20 percent by the end of this year. This has caused a sporadic panic of buying by middle to upper income housewives whose infants and toddlers depend on baby formulas. Some of those in the lower income class switched to soymilk which is lower in price and easily found at supermarkets and street food vendors.

Three types of consumer products that continue to dominate the market are powdered milk, sweetened condensed milk, and liquid-ready to drink milk. As of April 2007, consumption of liquid milk, powdered milk, and sweet condensed milk are growing by 20 percent, 10-12 percent, and 20 percent respectively.

A major milk processing facility in East Java is providing free milk for school children once a week in areas surrounding their facility in an effort to increase people's awareness of the health benefits of milk. They do this as a continuation of the USDA's School Milk program that was stopped in 2003.

TRADE

Indonesian imports of whole milk powder are estimated to be stagnant at around 27 TMT in 2007 and 2008 due to high prices on the international market and industry preference to use non-fat dry milk and anhydrous milk fat, because they have a longer shelf life and are easier to combine with other dairy products. Indonesian imports of non-fat dry milk are expected to increase to 161 TMT in 2008 mostly due to increasing consumption regardless of the price. Since the price of non-fat dry milk in the international market is skyrocketing, as a substitute to non-fat dry milk, Indonesian imports of whey are expected to grow by 30 percent in 2007 to 38,000 tons. Imports are expected to grow further should the price of powdered milk continue strengthening on the international market.

The drought that hit Australia and the decline of the export subsidy policy of the EU ended up increasing the price of powdered milk sourced from those origins, and have resulted in increased U.S. exports of dairy products to Indonesia, particularly non fat dry milk and whey powder. A prominent dairy processor which used to source its powder from its European based main office even reported that 50 percent of its dairy powder is now imported from United States.

However, given the long historical presence in the Indonesian market and geographical proximity, Oceania and the European Union are still enjoying about 60 percent market share, while the United States holds another 30 percent of the market share.

The dairy industry association also reported a change in dairy buying patterns. Now importers are hedging or drawing contracts with Australia to import frozen concentrated liquid milk with up to 45 percent Total Solid. Concentrated liquid milk is reported to offer lower price compared to powdered milk, yet provides a better taste.

STOCKS

Despite some delays in shipments, most of the prominent dairy manufacturers have covered their stock until January 2008, and some have even made contracts through the first quarter of 2008 in order to hedge against powdered milk high prices.

Non fat dry milk ending stocks are estimated to decrease to 9,000 tons in 2007 due to the strong demand from local manufacturers, tight supplies in exporting countries, and high prices in the international market.

PRICE

Product	Price (IDR)	Price (USD)
Local fresh milk Grade 1 (farm gate – 12% TS, 0 – 250,000/ml TPC)	3,047/kg	336/ton
Local fresh milk Grade 2 (farm gate – 12% TS, 250,000 – 500,000/ml TPC)	2,947/kg	325/ton
Local fresh milk Grade 3 (farm gate – 12% TS, 500,000 – 1 million/ml TPC)	2,847/kg	314/ton
Whole Milk Powder		5,200/ton
Non Fat Dry Milk		4,100/ton
Whey (CNF)		2,000/ton

Source: Union Of Dairy Cooperatives, dairy manufacturers, and traders

Note: Exchange rate: Rp. 9,072/USD1 as of July 2007.

Nowadays, the local dairy cooperatives are trying to adjust the price of fresh milk they deliver to the dairy processing industry to reflect the increasing price of powdered milk in the international market. This places further pressure on processors to increase their prices, which will limit growth in Indonesian milk consumption to 6 percent in 2008.

Previously, hygiene was not an important consideration because fresh milk was used to produce sweetened condensed milk. Milk processors are finding it difficult to source higher quality fresh milk. However, one major dairy company located in East Java provides farmers who have an agreement to deliver their fresh milk with a premium price if the fresh milk contains less than 250,000 bacteria/ml. This policy combined with a shorter milk delivery chain has managed to improve the quality of milk produced by these farmers. As a result around 52 percent of fresh milk produced by East Java dairy cooperatives is classified in Grade I, while another 38 percent is in Grade II.

II. PSD TABLES

PSD: NON-FAT DRY MILK

PSD Table									
Country	Indonesia								
Commodity	Dairy, Milk, Nonfat Dry						(1000 MT)		
	2006 Revised			2007 Estimate			2008 Forecast		
	USDA Official	Post Estimate	Post Estimate New	USDA Official	Post Estimate	Post Estimate New	USDA Official	Post Estimate	Post Estimate New
Market Year Begin		01/2006	01/2006		01/2007	01/2007		01/2008	01/2008
Beginning Stocks	14	14	14	12	12	12	9	9	9
Production	0	0	0	0	0	0	0	0	0
Other Imports	140	140	140	147	147	147	0	0	154
Total Imports	140	140	140	147	147	147	0	0	154
Total Supply	154	154	154	159	159	159	9	9	163
Other Exports	10	10	10	5	5	5	0	0	5
Total Exports	10	10	10	5	5	5	0	0	5
Human Dom. Consumption	132	132	132	145	145	145	0	0	147
Other Use, Losses	0	0	0	0	0	0	0	0	0
Total Dom. Consumption	132	132	132	145	145	145	0	0	147
Total Use	142	142	142	150	150	150	0	0	152
Ending Stocks	12	12	12	9	9	9	0	0	11
Total Distribution	154	154	154	159	159	159	0	0	163
CY Imp. from U.S.	26	26	36	28	28	34	0	0	46
CY. Exp. to U.S.	0	0	0	0	0	0	0	0	0

Note: Not Official USDA Data

PSD: WHOLE MILK POWDER

PSD Table									
Country	Indonesia								
Commodity	Dairy, Milk, Nonfat Dry						(1000 MT)		
	2006 Revised			2007 Estimate			2008 Forecast		
	USDA Official	Post Estimate	Post Estimate New	USDA Official	Post Estimate	Post Estimate New	USDA Official	Post Estimate	Post Estimate New
Market Year Begin		01/2006	01/2006		01/2007	01/2007		01/2008	01/2008
Beginning Stocks	14	14	14	12	12	12	9	9	9
Production	0	0	0	0	0	0	0	0	0
Other Imports	140	140	140	147	147	147	0	0	161
Total Imports	140	140	140	147	147	147	0	0	161
Total Supply	154	154	154	159	159	159	9	9	170
Other Exports	10	10	10	5	5	5	0	0	5
Total Exports	10	10	10	5	5	5	0	0	5
Human Dom. Consumption	132	132	132	145	145	145	0	0	154
Other Use, Losses	0	0	0	0	0	0	0	0	0
Total Dom. Consumption	132	132	132	145	145	145	0	0	154
Total Use	142	142	142	150	150	150	0	0	159
Ending Stocks	12	12	12	9	9	9	0	0	11
Total Distribution	154	154	154	159	159	159	0	0	170
CY Imp. from U.S.	26	26	36	28	28	34	0	0	46
CY. Exp. to U.S.	0	0	0	0	0	0	0	0	0

Note: Not Official USDA Data